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Project Report

BRITISH COLUMBIA FINANCIAL REVIEW: THE ISSUE OF DISPOSAL AND VALUATION OF ASSETS

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Executive Summary—Disposal and Valuation of Assets

This report is a comprehensive assessment of the way in which government values and disposes of public assets.

It concludes that, with the exception of higher profile dispositions, little attention has been paid to the effective management and adequate disposal of assets.

The government's higher profile privatizations have raised some public questions about the appropriateness of the transactions and their financial returns. Although due process was followed in the cases reviewed, in some of these sales the government failed to achieve its specific objectives.

For example the "Expo" lands at False Creek were put up for sale as a single block with the explicit objective to limit the residual obligations. However, the sale agreement actually entered into left the province with full, open-ended liability for the cleanup costs, which current estimates suggest could be more than 50 per cent of the sale proceeds. The report concludes that other options for disposing of the land might have been chosen: with the known uncertainty of clearing the site, it might have been more prudent to recognize and quantify the risk before selling the property, either in smaller lots or in one large lot.

The report proposes adjustments to the carrying values to reflect:

- The overstatement of future income from the False Creek Land sale by $18.3 million.
- The overstatement of the value of Duke Point lots by $0.5 million.

The report recommends that:

- Serious consideration be given to centralizing major asset disposal to:
  - Reduce duplication of effort.
  - Ensure that established valuation and sale procedures are followed consistently so that proper value will be recovered.
- The carrying value of future sale proceeds from the sale of False Creek land be reduced by $18.3 million.

The Issue of Disposal and Valuation of Assets

A. Summary of issues and entities involved

1. False Creek Land Sale

Primary and Subsidiary Issues/Recommendations—We reviewed the process by which the False Creek land was sold by British Columbia Enterprise Corporation (BCEC) and the carrying value of amounts still owed to the Province resulting from this sale. We have three main conclusions:

(i) If it is accepted that it was appropriate to sell the land in one block, due process was followed.

(ii) However, having established as an objective that it would limit the residual obligations to BCEC, the arrangements entered into did not meet this objective: those acting on behalf of the Province contracted to assume an open-ended unspecified liability (which could now turn out to cost the Province up to $100 million) by agreeing to undertake site remediation at the Province's cost.

(iii) The amounts receivable from the sale are over-valued in the accounts of the Province. The amounts receivable under the Concord note and the Public Participation Funding Agreement, both of which are included in the General Fund as part of Mortgages Receivable, should be written-down during fiscal 1991/92. The write-down of the Note Receivable is recommended in order to more accurately reflect the discount rate provided for by the note in the event of its prepayment. The write-down of the Public Participation Funding Agreement is recommended in order to reflect the current estimate of the present value of likely future payments based on total developable floor space of the site.

The recommended adjustments as at December 31, 1991 are as follows:

	December 31, 1991 ($000)		
	Carrying Value	Recommended Valuation	Proposed Write-down
Note Receivable	$107,597	$103,179	$ 4,418
Public Participation Funding Agreement	20,445	6,500	13,945
	$128,042	$109,679	$18,363

As an observation to this process, and with the benefit of hindsight, there were different options which might have been chosen: with the known uncertainty of clearing the site, it might have been more prudent to recognize and quantify the risk before selling the property, either in smaller lots or in one large lot.

Entities Involved/Related Issues—Appendix 2B to this paper, contains a full discussion of the issues and the circumstances surrounding the recommendations.

2. Crown Lands—Murrin Property

Primary and Subsidiary Issues—In October 1991, Crown lands agreed to acquire a former substation site in Vancouver's Chinatown for $9 million from B.C. Hydro (the property has not, to this point, been acquired). The site is known to contain contaminated soil and may require soil remediation work. The government reached an understanding with the the Chinatown Merchants Association that it would lease them the site for use as a parkade. A Memorandum of Understanding as to the essential lease terms indicate the rents will be below fair market value, particularly in the first five years of the 35 year term.

Impact on government recommendations

- Commencing in the 1991/92 Public Accounts, the commitment to acquire the property should be noted.
- The value of the property will likely be substantially less than its $9 million acquisition cost once the lease is signed, and as a result the carrying value should be written-down to a nominal value.
- The $9 million purchase price will be paid by way of a credit against 1991/92 Hydro dividends otherwise payable. This will decrease revenues from Hydro.
- The tenant would be responsible for current soil remediation costs, if any. However, the property reverts to the government at the end of the term, so that the government would still be exposed to potential future clean-up costs. No provision for these costs is recommended this time.

B.C. Hydro and B.C. Lands are involved, as discussed below.

3. Overall comment

The processes followed by ministries and Crown corporations are designed to result in the receipt of a fair price for the assets disposed. As a general rule, B.C. Lands is responsible for the disposal of all lands held by various ministries. Crown corporations carry out their own disposal processes. BCBC is responsible for the disposal of properties that form part of the accommodation pool provided to government by BCBC. Consideration should be given to centralizing disposal functions to reduce duplication of effort and costs and to ensure that sale processes are followed consistently. Direct disposal by Crown corporations appears reasonable for specialized assets where the best knowledge of values and potential buyers is within the corporation. Examples would be the disposal of ships by B.C. Ferry Corporation or rail cars by B.C. Rail. However, for assets which are not specialized, a central function should have responsibility for all asset dispositions, to ensure that benefits to the province are maximized.

B. Description/scope

1. Asset disposals

Asset disposals occur continually in government. Real property and other capital assets (houses, vehicles, equipment, furniture and fixtures and so forth) are disposed of on a regular and ongoing basis. In addition, certain assets are disposed of under specific initiatives. In the last four years the government's privatization initiative has resulted in the sale of certain government assets and the contracting out of certain service functions.

With respect to ongoing disposals, the purpose of our review was to identify issues that may require changes to the manner in which transactions have been reported or carried on the government accounts and to report on issues affecting future reporting within government.

Our review focused on the following:

- The disposal process policies of various entities.
- The appropriateness of the disposal process.
- Whether the process was followed in the more sizable transactions.
- Identifying on-going obligations or future costs related to transactions completed as well as transactions in process.

We reviewed the asset disposal process for the following entities:

B.C. Lands (Ministry of Environment, Lands and Parks)
British Columbia Buildings Corporation
Transportation and Highways
Government Services—Purchasing Commission
Energy, Mines and Petroleum Resources

Other entities:

Privatization Benefits Fund
False Creek (Expo Lands) land sale
B.C. Hydro (Mainland Gas Division)
WLC Developments
Duke Point Development Ltd.
Details of these are given in the Appendices.

C. Government policies and practices

Findings and conclusions

The policies and practices of government and the analyses and findings of the consultants are reported on separately for each entity we reviewed.

1. B.C. Lands—Ministry of Environment, Land and Parks

With respect to disposal, B.C. Lands' mandate is to strive to allocate Crown land to its most suitable use and achieve a fair return from the rent and sale of its resources through market based pricing.

Policies regarding the disposal of Crown lands are well documented and understood within government. The latest updated policies with respect to disposal are included in the policy manual "Crown Land Policy Summary, Spring 1991".

B.C. Lands' land management and land disposition services are delivered through eight regional BC Lands offices each of which has a reasonable degree of autonomy.

In the mid 1980s, B.C. Lands initiated a program to organize and monitor their inventory of lands. A computer database known as the Lands Inventory System (LIS) created a comprehensive listing of properties. Properties in the data base are classified either as newly acquired, holding, being prepared for sale or lease, or available for sale. Properties classified as available for sale or lease are automatically listed in a publicly available Crown Land Marketing Catalogue which is published two to three times per year. Daily printings of properties located within a region can be obtained.

It is the responsibility of the regional offices to identify properties that are suitable for sale to the private sector through consultation with regional and local authorities, other ministries and the private sector.

a) Methods of disposition

The overriding principle of disposal is that Crown lands are first offered through public competition before being offered through other means.

Methods used to dispose of Crown lands through public competition are as follows:

a) Public Lot Draw. This method is generally used for the initial offering of Crown land developed for residential or recreational use. It is mainly used for the sale of residential lots.

b) Public Auction. This method is generally used for the disposition of Crown lands suitable for agricultural purposes. The successful candidate is determined by way of a bonus amount that the bidder is willing to pay above the stated price or lease rate.

c) Public Offering. This method is often used to sell commercial and industrial properties, properties transferred from other ministries and miscellaneous dispositions. The public offering method is used where the property under question has a determined use. B.C. Lands establishes an upset reserve price in these cases, usually by means of an independent appraisal. This method is commonly referred to as "public tendering".

d) Proposal Call. This method is appropriate for larger properties that are available for development but do not yet have a determined use. Bids are evaluated not only on the basis of price but also on the basis of the merits of development proposal.

Methods used if public competition has not resulted in a sale:

i) Direct Sale or Lease. If a competitive public process does not result in a sale B.C. Lands may negotiate with interested parties on a first-come, first-served basis.

ii) Agency Sales Agreement. Certain properties may be listed in the MLS system directly by Regional Offices. B.C. Lands acts as the listing agent and the listings are distributed to real estate boards, which make them available to their members. The real estate agent who completes the sale is paid a standard commission. If no sale occurs within 90 days, an independent realtor may be selected as the listing agent.

b) Pricing and valuation

B.C. Lands' objective is to achieve market value in all dispositions to private interests. Independent appraisals are generally obtained to assist in establishing a price. Dispositions for public oriented purposes (i.e., to municipalities for parks or public buildings) are by free Crown grants. If there are historical book costs, the grantee has to pay these costs.

Properties transferred to B.C. Lands from other Ministries are usually transferred at their carrying value which, in almost all cases, is a nominal amount. Any sales to B.C. Lands from Crown corporations are generally made at market value. Inventory of land is recorded at the lower of cost and net realizable value. This can result in inconsistent recording of carrying values, depending on the original ownership. In spite of the inconsistencies it would, in our view, be inappropriate to write-up the properties acquired from other ministries to a more current value. This practice would result in the ability to manipulate the financial position of government and is contrary to generally accepted accounting principles.

Project development costs related to the inventory of land held for development are capitalized. The project officer is responsible for assessing the future revenues from the project and when those revenues will not recover the carrying value, a write-down of the property is made.

c) Property under development

At March 31, 1991 the General Fund Financial Statements showed $46 million in Property Under Development. This amount breaks down as follows:

Property Under Development		$46,733,172
Breakdown by Regional Office:		
Vancouver Island	$ 196,651	
Lower Mainland	34,382,105	
Thompson-Okanagan	4,946,318	
Kootenay	154,789	
Cariboo	1,910,607	
Skeena	5,083,470	
Omineca	1,853,261	
Peace	1,548,001	
Real Estate Services	95,828	
	50,171,030	
Provision for Asset Devaluation	(3,437,864)	
Rounding	6	
	$46,733,172	

Property under development in the Lower Mainland Region consists of approximately 150 individual items. The provision for asset devaluation of $3.4 million is composed of about a $2.6 million general allowance and $0.8 million related to specific properties. Staff at B.C. Lands believe that the provision is sufficient and results in an appropriate carrying value using the lower of cost and net realizable value principles. On the basis of our review and discussion, we agree with their viewpoint. No additional write-down or provision is necessary. The $2.6 million general allowance reflects conservatism in B.C. Lands' valuation approach and suggests that the risk of property under development being overvalued is low. At present, valuation assessments for each property are made annually by a project officer. Property under development is generally not valued by independent appraisal until it is marketed.

In fiscal 1989/90, property under development was written-down by $12.76 million. The write-down consisted of 135 individual items. Our discussions with B.C. Lands indicated that, prior to that write-down, the Ministry was not aggressive in identifying projects that should be written down. The write-down was made at the same time as the effort to improve the government's inventory of lands, and represented a clean up of the books. One of the larger items was a $1.5 million write-down relating to Westwood Plateau. Other writedowns included municipal land development and land servicing agreements that are primarily in rural and industrial areas where demand had fallen off.

d) Degree of development activity

As a general rule, B.C. Lands does not develop its surplus properties to be made available to the private sector. Lands suitable for residential subdivision are sold to the private sector for subdividing. Costs incurred in preparing a property for sale include the cost of appraisal, survey, marketing and access roads, where necessary.

There is currently no formal policy on site servicing costs. The appropriateness of incurring these costs is determined on an individual project basis. In the majority of projects, site servicing costs are not incurred.

e) Policy on representations and warranties

B.C. Lands endeavours to use a standard form Purchase and Sale Agreement in most transactions. Unique and high value properties sold through the process of negotiation may be sold under non-standard agreements.

The standard form agreement does not make any representation or warranty to the purchaser regarding:

- The fitness of the land for any particular use.

- The condition of the land environmental or otherwise, including the presence or absence of any hazardous or potentially hazardous substances on or under the land (and obtains an indemnity from the purchaser regarding possible environmental claims).

- The general condition or state of any utilities or other systems on the land.

Notwithstanding the standard form agreement, the question arises as to whether the government has any environmental liability for future clean-up costs of lands that contain industrial contaminants. More specifically, does the government bear any exposure on properties it has sold despite the presence of the disclaimer in the purchase and sale agreement? There are no clear fiscal parameters for making an assessment of this question.

See the Issues Report on Environmental Costs for further discussion of this matter.

f) Revenue forecasts

Revenue from the sale of Crown lands is forecast as follows for the next five years:

	$ million
Estimated 91/92	38.68
Forecast 92/93	38.80
Forecast 93/94	38.40
Forecast 94/95	38.10
Forecast 95/96	38.10

In the six month period from April 1, 1991 to September 30, 1991 actual sales totalled about $19.67 million.

g) Transactions examined

As part of our review we examined all transactions over $1 million completed in the 1990/91 fiscal year and to September 30, 1991 of the 1991/92 fiscal year. Additionally, we inquired about any significant transactions pending. We reviewed these transactions with the objective of determining whether B.C. Lands' policies were followed, if a sale had in fact occurred and if there were any ongoing obligations to the province.

i) Songhees, Victoria

Songhees is a former industrial parcel of land in Victoria's inner harbour which is now being marketed mainly for residential, commercial and hotel use. Three lots (4, 5 and 6) were sold to a single developer in May 1990 a fourth area was sold to the Provincial Rental Housing Corporation (PRHC) at 75 per cent of appraised market value. The sale of Lots 4, 5 and 6 followed the public offering process. Asking prices totalled $6.25 million for all three lots and they were sold for $5.84 million. The consideration consisted of cash and notes payable within a few months of issue.

The Songhees lands were previously leased for industrial uses and are known to contain some contamination. The Purchase and Sale Agreement with respect to Lots 4, 5 and 6 contained the standard representations and warranties as to the fitness and condition of the land.

ii) OMI, Mission

The Order Mary Immaculate (OMI) property in Mission was sold in May 1990 to a private company for $4.01 million cash. The method followed in effecting the sale was the proposal call process. An independent appraisal performed prior to the calling for proposals valued the property at $3.5 million.

iii) Marine Drive, West Vancouver

This property was transferred to the PRHC in July 1990 at $2.025 million being 75 per cent of "market value". Market value in this case was hard to determine as the property did not have any street access or multi-family zoning. In 1986 the property, without access or multi-family zoning, was appraised at $25,000. Since the PRHC will provide social housing the municipality agreed to provide access and the market value was greatly enhanced. In this transaction, "market value" was an agreed amount.

iv) 14.8 Acres in Surrey

B.C. Lands was approached by a private company that wished to acquire this agricultural land as part of an assembly for a proposed golf course. B.C. Lands had the land appraised (October 1990 at $535,000) and offered the property for sale by way of the public offering process. We examined the newspaper ads and the marketing package to evidence the public offering process. The property was eventually sold to a golf course developer for $1.14 million.

v) Blueberry Farm, Coquitlam

170.4 acres of agricultural land was sold to the lessee in October 1991 for $6,000 per acre or $1.022 million. An independent appraisal estimated the value of the land to be between $6,000 and $6,500 per acre. B.C. Lands sold the former Agricultural Land Reserve property to the lessee without offering the property to the public, which was consistent with the government's policy on dealing with lessees who had spent considerable funds on improving the land.

vi) Tranquille, Kamloops

The Tranquille property was the site of a long-term care hospital facility owned by the province that was closed in 1985. The site consists of 191 hectares of farmland containing over 40 institutional buildings and houses. The province decided to sell the property on an "as is" basis even though most of the buildings would be of no use or value to most prospective purchasers. The property was offered for sale in 1986 (or perhaps 1987) via a request for proposal. Little interest was generated and no sale occurred. In 1989, the property was again unsuccessfully marketed to the public under a request for proposal. Early in 1991, a private company was engaged to act as a listing agent and to auction the property. An asking price of U.S. $8 million and an auction date of June 26, 1991 were established. (The October 1989 independent appraisal estimated the value of the property to be between $6.5 and $7.5 million.)

An expression of interest was received relatively shortly prior to the auction date, no other interested parties have been identified. The government determined the expression of interest was sufficient to cancel the auction process and negotiate exclusively with the interested party. On August 15, 1991, a Purchase and Sale Agreement was signed for the sale price of $8 million. The consideration to be paid was as follows:

Cash	$ 300,000
Takeback Mortgage	7,700,000
	$8,000,000

Given the lack of interest generated from marketing initiatives over a five year period and lack of auction registrants, the cancellation of the auction and negotiation with the interested party was, in our view, a prudent step to take in the process.

The takeback mortgage calls for three principal-only payments of $300,000 on November 1, 1991, February 1, 1992 and May 1, 1992; interest at 9 per cent commences on May 1, 1992 and blended principal

and interest payments of $170,154 are thereafter made at the end of each quarter. The balance is due August 1, 1995 and there is an incentive for early payment of the outstanding balance as follows:

- Principal reduced by $750,000 if paid by August 1, 1994
- Principal reduced by $1,500,000 if paid by August 1, 1993.

For accounting purposes B.C. Lands recognized sales revenue of $6.5 million and set up deferred revenue of $1.5 million which will be recognized when the prepayment dates pass.

From a financial recognition point of view, the present value of the mortgage is less than its face amount due to the interest free period until May 1, 1992. All the imputed interest would be earned by May 1, 1992, so the net impact on fiscal 9191/92 finances is minimal.

The accounting treatment reasonably reflects the substance of the transaction. The collectibility of the proceeds does not appear to be an issue the administrator of the mortgage stated that the November 1, 1991 payment was made on time.

The property is known to contain ten capacitors which may contain PCBs. They are listed and appended to the agreement. This notwithstanding, the agreement contains standard warranty clauses in that the Province makes no representation or warranty regarding the fitness or condition of the lands.

vii) Murrin, Vancouver

B.C. Lands is negotiating to acquire a property in fiscal 1991/92 from B.C. Hydro at a price of $9 million being an estimate of market value established by B.C. Hydro. The Murrin property is located in Chinatown and is a former Hydro substation site with soils that are known to be contaminated. B.C. Lands decided to acquire the site when B.C. Hydro could not reach a sale agreement with the Chinatown Merchants Association (CMA) and the City of Vancouver. It appears that the government of the day made a decision that they would facilitate CMA in gaining use of the property for a parkade.

On September 11, 1991, the then Premier committed the province to lease the Murrin site to the CMA on favourable terms. In a subsequent Memorandum of Understanding between CMA and the province, the province committed to the essential terms of the lease which included:

- A term of 35 years.

- Annual rent of $10 for the first 5 years.
- Thereafter, annual rent equal to the excess, if any, of revenues over operating expenses and amortization of the development and construction costs.
- CMA to perform any soil remediation required.
- Reversion to the province at the end of the term.

Treasury Board approval of the transaction was received on October 10, 1991 subject to three conditions:

i) Payment by the government of the $9 million purchase price to Hydro by way of a credit against 1991/92 Hydro dividends otherwise payable.

ii) Rents (to tenants) in the new development are to be at market rates.

iii) The province sharing in any excess net revenues (it is unclear as to whether this would take effect from inception of the lease).

However, these approvals did not address all of the outstanding issues between B.C. Hydro and the Province. As a result, there is still no signed Offer to Purchase. However, the following issues flow from the transaction:

- The net realizable value of the property may be less than $9 million.
- Possibly an accrual for site soil remediation liability should be considered.
- For forecasting purposes, the dividends from B.C. Hydro will be $9 million lower than anticipated.

This transaction is still under negotiation, but some preliminary conclusions to the Murrin property issues are:

- A precise assessment of the property's fair market value would be difficult unless forecasts of rents to the Province for years 6 through 35 are available. However, although the property has a value of $9 million without the lease in place, it appears that the existence of the lease will reduce that value to a nominal amount. As a result, once acquired, it should be

written-down to nominal value. It is our understanding that a formal lease agreement has not yet been signed.

- CMA must bear the cost of any current site remediation, so the province is probably not at risk until the end of the lease. Thirty-five years may be a sufficiently long period of time to mitigate the present value of any likely remediation costs. No accrual is recommended.

- Recognition of a $9 million decrease in dividend from B.C. Hydro for fiscal 1992/93 is recommended in the revenue forecast, if not already recognized.

2. British Columbia Buildings Corporation (BCBC)

BCBC is the sole provider of accommodation to government. As a result, it carries out a significant number of real estate disposal transactions. Furthermore, the closure or planned closure of four institutions: Oakalla, Woodlands, Riverview and Jericho Hill, has given BCBC the opportunity to dispose of large parcels of land located within Greater Vancouver neighbourhoods.

a) Methods of disposition

The methods used by BCBC in identifying surplus assets and disposing of them have been outlined in the BCBC entity report.

The marketing methods used by BCBC are essentially the same as those used by B.C. Lands and include public tenderings, public offerings and listing agreements with real estate agencies.

The objective of BCBC, even in transfers to the Crown, is to receive disposal proceeds equal to fair market value. Some transfers, to municipalities, for example, are made at an agreed amount which may be less than market value (usually only a nominal discount to market).

b) Degree of development activity

It is the policy of BCBC not to construct buildings for sale to the private sector. The degree of land development activity undertaken by BCBC has increased since 1986 largely because of the four large former institutional properties that BCBC is presently preparing for disposal. This course of action has been, in part, influenced by the experiences of government in past transactions including the Expo Lands, the Westwood Plateau and Tranquille. It is the view of BCBC that, in order to achieve market value, it is prudent for the existing owner (BCBC) to take development properties through the rezoning process and receive the substantial increase in value that accrues after achieving the rezoning. There are no formal written policy guidelines on

the nature and amount of property development that will be undertaken on a project. BCBC management has (on the basis of information provided to its Board of Directors) sought the Board's approval to follow a particular course of action or to expend significant funds. While BCBC management wishes to maximize the return to the government in its property disposals, it realizes it is not in the business of developing real estate for sale to the private sector. In its view, this function is more appropriately performed by the private sector, so that BCBC's development activities generally stop at the rezoning and subdivision stage of development including offsite servicing.

c) Policy on representations and warranties

BCBC's policies on representations and warranties are essentially the same as those of Crown lands. However, its policy is to permit more flexibility and autonomy than a government ministry. Thus BCBC uses the standard clauses as an initial position from which it may negotiate. BCBC's management, which operates under a Board of Directors, enables it to have the flexibility that would be expected to be found in the private sector.

d) Revenue forecasts

Proceeds from property sales were $18.4 million in fiscal 1990/91.

The original forecast for 1991/92 was for $9.3 million in property sales. However, from April 1, 1991 to December 16, 1991, only $306,000 of sales have occurred. The revised forecast for the balance of fiscal 1991/92 amounts to $4.4 million, bringing the 1991/92 total to $4.7 million. The reasons for the negative difference are the economic recession having a greater effect than forecast and several large properties not selling as anticipated (800 Cassiar Street, Carey Road Group Home Victoria, Silverton and Cassidy Highway Works Yard).

The forecast revenue for fiscal 92/93 is $7.17 million. This does not include revenue from Planned Disposals discussed below. None of the planned disposals of former institutional properties are forecast to occur before 1993.

e) Completed transactions

As part of our review we examined all transactions over $1 million completed in the 90/91 fiscal year and to December 16, 1991 of the 1991/92 fiscal year (a total of three transactions). We reviewed these transactions with the objective of determining if B.C. Lands' policies were followed and if there were any ongoing obligations to the province.

For each of the completed transactions we examined the "request for appropriation" which is the authorization form signed prior to incurring marketing costs and bringing the property forward for sale. We also examined

the "disposition justification report" signed by the department which outlines the reasons for sale and the proposed method of sale.

In each case, the process followed was in accordance with expressed policies and there are no apparent ongoing obligations assumed by government.

f) Planned disposals

We reviewed files relating to the four institutional properties which are in the process of being prepared for disposal. The Woodlands, Riverview and Jericho Hill projects are all at very preliminary stages in the process. In each case, requests for funding for expenditures to be incurred have been limited to consulting and appraisal fees in order that BCBC determine an appropriate course of action it might follow.

The following is a summary of the projects at their stages of development:

i) Oakalla, Burnaby

The Oakalla property is a former penitentiary site in Burnaby consisting of 67.9 acres that slopes down to Deer Lake. After dedications to roads and public uses, the development site is 49 acres, of which BCBC owns 45.6 acres. The redevelopment plan for the Oakalla property calls for a mixed density residential development. The rezoning and development process for the property commenced in 1987. BCBC proposes to develop the property to the subdivision and off-site servicing stages before the property is offered for sale on a developable parcel basis. Our examination of BCBC's Oakalla files noted documentation for Board approval of courses of action and significant expenditures.

ii) Woodlands, New Westminster

The 67 acre Woodlands site houses Queens Park Hospital and an institution for the mentally and physically handicapped. BCBC is currently in the early stages of the comprehensive planning process. BCBC intends to subdivide the site into smaller plots and to provide offsite servicing to the plots for private sector developers.

The closure of these two institutions is under review by the current provincial government.

iii) Riverview, Coquitlam

This project encompasses the development of the Riverview mental hospital site into a comprehensive residential development. The Ministry of Health still occupies the hospital, but is making plans to vacate it. The full site is 245 acres. A 78 acre portion of the property

could be developed even if the Ministry of Health still occupies the hospital. The January 31, 1992 book carrying cost of the 78 acre portion is projected to be $330,000. To date the only significant activity on this site has been the commissioning of an independent consultant's report entitled "Concept For Land Value Estimation."

iv) Jericho Hill, Vancouver

The Jericho Hill site houses the Jericho School for the Deaf and the Justice Institute and is located west of the Department of National Defence's property and south of 4th Avenue. The School for the Deaf will be relocated in January 1993 and the Justice Institute will also be relocated although the date has not yet been determined. BCBC has started the consultation process with the City of Vancouver and intends to move into comprehensive development planning in 1992.

g) Legacy fund

The government is considering the establishment of a Legacy Fund under the Societies Act into which gains from the sale of large former institutional properties would flow. At present, this would involve the Riverview and Woodlands sites projects which will not be brought to market until 1993 or later. The concept is to create a fund that would be used to replace large institutions with regional and neighbourhood care facilities. As currently proposed, this fund would be governed by a Board of Directors with representatives from the Ministries of Finance and Corporate Relations, Social Services and Health.

The two main proponents of the Legacy Fund have been the Ministry of Social Services and the Ministry of Health. A Treasury Board submission has been prepared, but the new Cabinet has not yet made a determination as to whether to continue to phase out the large institutions for the physically and mentally handicapped.

3. Transportation and Highways

We reviewed two elements in the Ministry of Transportation and Highways ("Highways") the processes followed in the disposal of surplus land and the process followed in the second round of privatization of highways service contracts.

a) Surplus land

In 1988, Highways was identified as possibly being in possession of a large number of parcels of land which were surplus to their needs. A two-fold initiative was undertaken to identify the surplus lands and to streamline Highways inventory of its land holdings. An individual was engaged, under contract, to identify surplus lands. Lands identified as surplus are transferred

to Crown lands for inclusion in the Crown lands Inventory Process and eventual disposal.

The individual engaged to identify surplus lands provided a status report as at November 30, 1991. He has identified 1,194 potential surplus plots of land. Regional office staff will make a decision as to whether the plots are in fact surplus to Highways' requirements. To November 30, 1991, 136 plots had been determined by the regional offices to be surplus to their needs.

The second part of the initiative, the streamlining of the Ministry of Highways land inventory, has not yet been undertaken. Only "fee lands" are on record in the Land Title Office. Generally, these properties encompass only those acquired since the 1940s. Highways has been acquiring property since before the turn of the century. Further, Section 4 of the Highways Act states that the corridor serviced by Highways is deemed to be a highway. Of the 44,000 km of highways in the province, about 18,000 km may belong to Highways as a result of Section 4, but Highways has no recorded legal title to the property which thus cannot be readily inventoried. A general design of a Property Acquisition and Inventory Management System for Highways has been prepared but no funding approved for the $800,000 implementation cost.

It appears that the perception that Highways could contain a vast amount of valuable surplus land that is readily marketable is not well founded. Highways almost exclusively holds rural properties. Road corridors inside municipal limits are the property of the municipality. Therefore most of Highways' 44,000 km of roads are strung between the cities and towns of the province.

Highways periodically acquires houses and other buildings when obtaining land for highway corridors. These buildings are transferred to the Purchasing Commission for disposal (see below).

b) Highway service contracts

Initial Process—Between September 1988 and April 1989, the government privatized all the Province's road and bridge maintenance contracts. The objective of the government was to privatize a service function that could be performed by the private sector and achieve a cost savings to government in doing so. The province was divided into 28 contract areas, and a public proposal call process was held to secure the contracts. Contracts were awarded to 20 firms, ten of which were owned by former ministry employees. Highways signed a uniform three-year contract in each area. Forecast analyses performed by the government in 1988 demonstrated that $21 million in cost savings would be achieved over the duration of the initial three-year term of the contracts.

As a condition of each original contract, the contractor was obliged to offer each maintenance employee a job. Of the 2449 road and bridge maintenance employees, 2187 chose to work for the private contractors.

Second Round—The second round of proposals for the three-year contracts was issued in 1991. By early December 1991, contracts in 26 of the 28 regions had been negotiated. Negotiations on the remaining two are expected to be completed in early 1992. The objective in the second round is similar to that for the first (i.e., privatize a service function to produce a cost saving to government). Under the second round of proposals, the government tightened up some of the service standards and codified what were previously administrative practices.

Of the 26 contracts signed, 12 are with new contractors for a given contract area. Six of the ten companies owned by former Highways employees have been successful in second round bidding. On average, three bids were received for each contract area; only one contract area, Central Kootenay, had a single bid. Highways' management has indicated that the average increase achieved on the second round contracts has been well below the increase in inflation (16 per cent as evidenced by the change in CPI) over the same period. It should also be noted that in the view of Highways, the level of service required in the second round of contracts is generally higher than the first. Our observations lead us to conclude that the competitive bid process followed by Highways was effective in achieving the government's objectives.

A condition of the second round of contracts is that a replacement contractor must offer employment to all non-management, non-supervisory personnel of the out-going contractor at the commencement of the contract.

4. Purchasing Commission

The Purchasing Commission ("the Commission") operates within the Ministry of Government Services (formerly Ministry of Womens Programs and Government Services and Ministry Responsible for Families). Under a program called Warehousing and Asset Investment Recovery ("WAIR"), the Commission is responsible for reallocating identified surplus assets (such as furniture and industrial equipment) among various ministries and to the extent the assets are not suitable for reuse, selling the surplus assets, primarily from sales/warehouses located in Surrey and Victoria. Its selling methods are designed to obtain the best value for the surplus assets at the least cost to government and include:

- requests for proposal
- auction
- direct sales
- cash and carry

The Commission also acts on a fee-for-service basis as an agent for Crown corporations, ministries and MUSH agencies, on the disposal of certain assets.

The WAIR program operates on a cost recovery basis its revenues for fiscal 1990/91 of approximately $2.95 million were approximately $1.5 million short of its expenditures resulting in a program deficit of that magnitude. The program's restated budget for the fiscal year ending March 31, 1992 projects revenues of approximately $4.38 million, which amount is expected to fully cover the program's costs. Similarly, projected revenues of some $4.68 million for fiscal 1993 are expected to cover program costs.

According to the management group for the program, the process for disposing of surplus assets is well defined and operates effectively. The issues in the program result from the lack of incentive for various ministries to identify redundant assets in order to effect proper asset management . Other than for replacement assets, no proceeds go to the ministry which controls the assets. Redundant assets which are not identified for sale result in a loss of cash flow from proceeds and in some cases, storage costs also result. Decentralized ownership structure for the various assets owned by government can result in inefficiencies such as the purchase of equipment by one ministry or agency while another has the same piece sitting idle. The extent of these inefficiencies and the cost to government is not easily quantifiable. It may be appropriate for government to conduct a further study to determine the extent of all the costs of the perceived inefficiencies.

5. Energy Mines and Petroleum Resources ("EMPR")

The general objective of EMPR is to facilitate private sector exploration and development of natural resources and then derive revenue from developed properties through royalties and income taxation. EMPR does not dispose of real estate or any significant amount of capital assets. Petroleum and natural gas resources are generally the property of the Province and are tenured to the private sector through leases. The Petroleum and Natural Gas Act provides the regulations as to the process the province must follow in leasing interests in these resources. Briefly, lease interests are acquired by the private sector through a closed bid competition conducted once a month. Private companies and individuals can request areas be brought to auction. Generally, leases run four to ten years and are maintained by paying a rental and conducting a certain amount of exploration. If the lessee finds oil and gas, it is entitled to retain the rights to the commercial use of the property.

Mineral rights are administered in a different manner than oil and gas lease, and again do not involve outright sales to the private sector. Licensed miners can stake a claim on any unclaimed Crown lands or privately owned land. Claims gave them the right to explore and develop mineral interests, which are registered with the Province. In this manner, the government completely relies on activities of the private sector to generate revenue from mineral resources by developing commercial mines and then reaping the royalty and taxation income. The Mineral

Tenure Act provides the regulation to the process and details rules governing the use and occupancy of the surface for mining purposes.

Based on discussions with the EMPR staff in charge of petroleum and gas tenures and mineral rights, it does not appear there are any asset disposal or valuation issues within the Ministry.

6. Other entities

Following our review of other entities, a number of other disposal issues came to light. These are discussed below.

a) **Privatization Benefits Fund**—See Appendix A.

b) **False Creek (Expo lands) sale**—See Appendix B.

c) **B.C. Hydro**—Privatization of Mainland Gas—See Appendix C.

d) **WLC Development Ltd**—See Appendix D

e) **B.C. Pavilion Corporation**

Issues identified:

- Bridge Studios, which does not give an economic return to government, should be considered for alternative uses, even sale.

- The carrying value of B.C. Place Stadium is not supported by its current earning capability. In spite of this, there should be no write-down of the asset since there were significant economic spin-offs.

f) **B.C. Rail**

The carrying value of B.C. Rail's investment in Northeast Coal may require adjustment in the future. There were no other issues with respect to asset disposition and/or valuations identified.

g) **Discovery Foundation**

Accounting policy with respect to recording of investments at net realizable value and charging of allowance for doubtful investments against contributed equity needs to be reviewed.

7. Privatization Process—Office of the Auditor General

To avoid duplication we have not (except in the specific circumstances noted above) reviewed transactions that have already been reported on by the Auditor General nor have we commented on the issues identified by him. We have, however, reviewed the audit reports issued by the Auditor General on the privatization process and transactions included in the Auditor General reports of 1989, 1990 and 1991 in order to gain an understanding of his reviews and his conclusions. Where necessary, we discussed the work performed by the Auditor General, the rationale for selecting the study subjects as well as the conclusions reached with Peter Gregory, Executive Director in the Auditor General's Office.

The Auditor General has, since 1989, reported extensively on the privatization process, including the review of specific transactions, in his annual reports and in his value-for-money audits. His comments and conclusions are found in each of the 1989, 1990 and 1991 reports.

A summary of the studies completed by the Auditor General in the last three years is shown in Exhibit I.

Exhibit I
Summary of studies completed by Auditor General

Report	Purpose	Overall Conclusion
Privatization: The Process	An assessment whether the stated process is adequate to provide information needed to evaluate value-for-money consequences of privatization decisions.	Process adequately considers value-for-money when public bids are received.
Early initiatives: Queens Printers publication Section Kelowna soil lab Langford sign shop	Examine process followed and assess whether value-for-money information was obtained.	No public bids as each entity sold to employee groups; Value-for-money information was not obtained.
Southern Vancouver Island highways contract	(same as above)	Process was adequate to achieve value-for-money information since a public bidding process was followed.
BCEC loans portfolio	Assess whether BCEC obtained fair market value-for-loans sold.	Yes.
BCEC Westwood Plateau	Examine the process followed and assess whether value-for-money information was obtained.	Yes, but financial analysis in making the decision to sell the property in one parcel was lacking.
Acquisition and Divestiture of Land	Assess whether the process established to dispose of real estate properties ensure value-for-money is achieved and determine if policies are being followed.	Yes, policies are appropriate and they are being followed.
Reporting the Results of Privatization Transactions	Assess whether the appropriate financial reporting of privatization transactions has occurred.	PBF Act complied with, but definition chosen to determine gains from privatization questioned.
Standards of Road and Bridge Maintenance	Do standards in contracts meet industry standards and are roads in safe driving conditions.	Standards meet industry standards and practices; Highways study needed to determine if roads are in safe driving condition.
Monitoring of Road and Bridge Maintenance Contractors	Does highways have system in place to monitor and evaluate contractor performance.	Quality Assurance Program provides a reasonable approach but improvements are required.

Appendix A

Privatization Benefits Fund

A. Description

1. Mandate

The Privatization Benefits Fund ("the Fund") was established in 1988 for the purpose of holding, in perpetuity, the proceeds from assets disposed of through the privatization program.

The Fund is an investment fund as opposed to an operating fund and, as a result, has its own accounting policies and makes its own investments. It is permitted to make investments provided for under Section 36(1) of the Financial Administration Act. In addition, the Minister of Finance and Corporate Relations ("Minister of Finance") may invest money that is in the Fund in any investment of a class that is approved by the Treasury Board, including domestic and foreign equities, mortgages, real estate, corporate bonds and venture capital.

Where the government receives the "proceeds" of a "privatization transaction" that has been designated as such by the Lieutenant Governor-in-Council, the Minister of Finance must pay all or a portion of the proceeds (as may be specified by the Lieutenant Governor-in-Council) into the Fund. The Minister of Finance, provided he is so directed by the Lieutenant Governor-in-Council, may pay all or part of the accrued earnings of the Fund into the General Fund to be used for either the purposes of deficit reduction and/or general program purposes.

2. Size of organization

As outlined in Schedule 2, the net equity of the Fund as at March 31, 1991, was approximately $497 million: The Fund is expected to have a projected value in excess of $550 million at its March 31, 1992 fiscal year end (Schedule 2 following). Investments made by the Fund are accounted for on a market value basis.

The administration, accounting and investment functions for the Fund are carried out by the Provincial Treasury on behalf of the Minister of Finance and Corporate Relations.

The Fund's overall investment objectives and investment criteria are established by the Minister of Finance and the Treasury Board. An advisory board (the "Treasury Advisory Board") makes recommendations on investment policy and strategy issues to the Minister of Finance who has ultimate authority to make the investment decisions. The Treasury Advisory Board consists of five external members, the Minister of Finance and the Deputy Minister of Finance. The Investments Branch of the Provincial Treasury makes the day-to-day investment decisions for monies held within the Fund. The Fund also engages external fund managers to provide it with investment management and advisory services. Seven different fund managers currently provide services to the Fund.

3. Legal basis

The Fund was created under the authority of the Privatization Benefits Fund Act in 1988 (Bill 17—1988). Originally, all of the investment proceeds were to be paid to the General Fund for purposes of deficit reduction or general purposes. In 1990, the Act was amended to provide that accrued earnings of the Fund could only be paid to the General Fund at the direction of the Lieutenant Governor-in-Council and only in such amount as he might direct. The Fund is not otherwise permitted to pay out any amount of its capital and/or income.

4. Subsidiary entities

The Fund has two wholly owned subsidiaries WLC Developments Ltd. (W.L.C.) and Duke Point Developments Limited (Duke Point). The subsidiaries were acquired by the Fund on August 31, 1989 from the British Columbia Enterprise Corporation (BCEC) approximately one month prior to BCEC ceasing operations and transferring its remaining assets, liabilities, rights, etc. to the province and to B.C. Pavilion Corporation.

WLC and Duke Point are the subject of separate reports in the Appendices.

5. Recent history

The Fund's mandate is to receive "proceeds" from transactions designated by the Lieutenant Governor-in-Council as "privatization transactions". To date, the Lieutenant Governor-in-Council has designated the transactions outlined in Schedule 1, following, as privatization transactions for purposes of the Fund.

Since its inception in 1988, the Fund has received net proceeds from the foregoing designated privatization transactions, has invested those funds and has paid dividends to the General Fund (for fiscal 1989 and fiscal 1990 only). Schedule 2 outlines the proceeds received by the Fund, their sources, the amounts of dividends paid to the General Fund, and the results of its performance since inception.

Schedule 1
Privatizations designated By OIC

Kelowna Soil Laboratory	(OIC #1269/88)
Sunshine Hills Golf Course	(OIC #1269/88)
Langford Sign Shop	(OIC #1269/88)
Expo Land Sale	(OIC #1269/88)
Three E Training	(OIC #1971/88)
Alpha Hydrographics	(OIC #1971/88)
Wakefield Accoustics	(OIC #1971/88)
Telkwa Forest Nurseries	(OIC #1971/88)
Victoria Highway Maintenance	(OIC #1971/88)
BC Hydro Rail and Gas Divisions	(OIC #2197/88)
Highway Maintenance Districts	(OIC #2297/88)
Image Media Services Limited	(OIC #2297/88)
Highway Maintenance Districts	(OIC #333/89)
Environmental Laboratory	(OIC #333/89)
Forest Nurseries	(OIC #333/89)
Food and Diary Lab	(OIC #333/89)
Energy, Mines and Petroleum Publications	(OIC #333/89)
Aggregate Screening Equipment	(OIC #333/89)
Highway Maintenance Districts	(OIC #459/89)
BC Enterprise Corp. Land Sales	(OIC #459/89)
BCEC Operating Dividend	(OIC #459/89)
Koksilah	(OIC #1421/90)
Shaw Maintenance, etc.	(OIC #486/89)
Extension of Highway Privatization— Lease Equipment Proceeds	(OIC #1076/91)

Schedule 2
Privatization benefits fund carry forward schedule ($000)

	March 31 1989	March 31 1990	March 31 1991	March 31 1992 (Forecast)
PROCEEDS				
1. B.C. Hydro				
a) Mainland Gas & Rail Divisions	$220,270	$7,893	$9,687	$581
b) ViGas Division				5,100(3)
2. BCEC				
a) Expo Lands	5,352			
b) Operating Dividend	37,811	6,258		
c) Westwood Land Sale		55,125		
3. Government				
a) Road and bridge maintenance	36,460	14,922	12,554	10,300
b) Forest nurseries	5,527			
c) Sunshine Golf Course	975			
d) Langford Sign Shop	835			
e) Environmental Laboratory	850			
f) Media Centre	62			
g) Food and Diary Lab	216			
h) Soil laboratory	138			
i) Other	22	199		
Proceeds Received	308,518	84,923	22,241	15,981
INVESTING/OPERATING ACTIVITIES				
Investment Income	12,928	39,486	30,400	34,330
Dividends to General Fund	(12,928)	(11,592)		
Management Fees		(72)	(528)	(580)
WLC Income		9,118 (1)	281	3,987
Duke Point Income (Loss)		(2,465) (1)	394	338
Contributed Surplus		19,000 (2)		
Change in Unrealized Appreciation (Depreciation)		(15,000) (2)	12,470(2)	(4)
Increase in Equity	308,518	123,398	65,258	54,056
Ending Equity	$308,518	$431,916	$497,174	$551,230

1. From September 1, 1989 to March 31, 1990.
2. The Contributed Surplus results from PBF's investments in WLC and Duke Point; the unrealized Appreciation (Depreciation) results from the market valuation of assets owned by the Fund at its year end.
3. This amount has yet to be designated
4. Market value at March 31, 1992 unknown.

6. Reporting and accountability

Only those transactions which have been designated as privatization transactions are included in the Fund.

The Banking/Cash Management Branch of the Provincial Treasury is responsible for accounting for the proceeds received by the Fund and the results of its investment decisions. Part of its role is to ensure that the appropriate proceeds are paid to the Fund on a timely basis. When the privatization initiatives were originally carried out, the Privatization Committee reviewed privatization proposals and reviewed the determination of "proceeds" for purposes of the Fund.

The Treasury Board approved the definition of "proceeds" for the purposes of the Fund in order to recognize the "one time nature of the revenues received and, at the same time, ensure that the effects on the General Fund are neutral". As outlined in the notes to the Fund's financial statements for its fiscal year ended March 31, 1991, "proceeds" of a privatization transaction are defined as the selling price (net of selling costs), minus the book value of the assets sold. Only those transactions where selling costs and book value were less than the selling price (i.e., there was a gain on the privatization), resulting in payment to and recording by the Fund.

The Fund is not permitted to pay out any of its capital or income (except for such part of its income that is directed by the Cabinet). As a result, a certain portion of the proceeds of designated privatization transactions have been held back pending resolution of pre-identified issues and contingencies. For example, $50 million was withheld from the proceeds of the Mainland Gas and Rail division privatization by B.C. Hydro for funding of potential pension liabilities. Approximately $15 million of this amount was paid to the Fund. The balance was paid to the B.C. Hydro Pension Plan in accordance with actuarial recommendations. Where costs have not been identified prior to monies being paid to the Fund, they have become obligations of the General Fund. It is our understanding, based on discussions with Provincial Treasury, that except for the issues raised by the Auditor General (see below), there have been no significant post-contribution costs that have been borne by the General Fund.

In his 1990 report entitled "Reporting the Results of Privatization Transactions, A Review of the Government's Reporting of the Financial Results of Privatization Transactions," the Auditor General reported that the Government's accounting for the 46 sales designated by Cabinet as privatization transactions to March 31, 1989 "complied in all material respects with the provisions of the Privatization Benefits Fund Act and with the Government's stated accounting policies". He did, however, question the accounting policy adopted by B.C. Enterprise Corporation which included present value of certain conditional payments resulting from the Expo Lands sale, thus enabling a payment of $5.4 million to be made to the Fund. (See separate appendix dealing with False Creek Lands.)

The Auditor General has issued an unqualified audit opinion on the 1991 financial statements of the Fund.

7. Financial controls/investment strategy

The role of the Banking/Cash Management Branch of the Provincial Treasury is to account for the proceeds that become payable to the Fund as well as to record the results of investment decisions made by the Investments Branch.

Investment decisions are governed by the investment criteria set out in Section 36(1) of the Financial Administration Act. The Minister of Finance is, however, permitted to diversify the investments of the Fund into additional classes such as equities (domestic and foreign), mortgages, real estate, corporate bonds and venture capital.

The Minister of Finance has approved certain classes of investments on the basis of the above criteria established by the Fund, and the investment ranges for them (within a tolerance level of 5% of the upper range). The investment classes, investment ranges and actual investment mix at September 30, 1991 are shown in Schedule 3 (shown on page 7).

The Fund has committed to provide $10 million to a merchant banking pool (Canadian American Investment Corp.) which has been established to provide capital for management buy-outs and for non-hostile takeovers. The pool has been in existence for two years but has not yet found a suitable investment.

The effect of these policy decisions will be to increase the investment risk for the Fund. In particular, the investments by the Venture Capital funds designed to provide expansion capital will result in potential for investment losses. Those which are successful, however, are expected to provide a commensurably higher rate of return to offset the risks. According to the Investments Branch of the Provincial Treasury the expected return from the venture capital investments is in the range of 15%—20%, after giving effect to possible losses.

Schedule 3
Investment classes, ranges and actual mix (at market value)

Asset Class	Approved Range %	September 30, 1991 %
Short Term	0-30	30.0
Bonds		
Government	0-30	26.1
Corporate	0-20	4.6
Canadian Equity		
Passive	0.30	9.4
Active	0-30	16.0
Foreign Equity		
Passive	0-10	6.7
Active	0-5	0.4
Mortgages	0-5	
Venture Capital		0.3*
WLC and Duke Point		6.5

* *In September 1991, as part of the diversification of the Fund's investment portfolio, the Minister of Finance approved investments of up to $20 million in aggregate ($10 million each) in two newly created venture capital funds designed to provide expansion capital to the private sector. The Fund's investment in the two new funds will be matched by funding from the private sector. The two identified investment managers (Ventures West and Canadian Corporate Funding Limited) are currently seeking capital from the private sector. They have been given a six month time frame within which to raise the capital.*

8. Management structure and issues

► Management structure

The overall responsibility for the Fund rests with the Minister of Finance. The day-to-day responsibility for its management rests with the Provincial Treasury.

► Accounting for privatization transactions

The Treasury Board approved the policy on revenue recognition and reporting to separate the one-time revenues of the government resulting from privatization from ongoing operations of the General Fund. It recognized the need for public policy underlying the formation of the Fund to ensure that all proceeds paid into the Fund were determined on a consistent and rational basis. Its purpose was not to account for the proceeds on a project basis.

The Auditor General, in his 1990 report, concluded that the Fund had, in all material respects, accounted for the designated privatization transactions in accordance with the Act and the policies approved by the Treasury Board. In his view, however, "the financial results of privatization transactions were not reported in the most appropriate manner"; a project basis of accounting for all privatization transactions would have been more appropriate in the circumstances.

The essential differences between the method of accounting approved by Treasury Board and that suggested by the Auditor General would have resulted in the recognition of a broad category of costs not otherwise recognized to offset revenues from privatization transactions as well as the recognition of losses which, in the end, would have resulted in a lesser amount of proceeds becoming payable to the Fund. The quantification of differences would require an in-depth study which is beyond the scope of this engagement.

However, one of the key types of costs not included in determining the net proceeds of the False Creek land sale was the cost of cleanup of the Expo Lands which is the province's responsibility. Current estimates suggest these costs would be more than $50 million, $18 million of which has already been incurred. These costs have been charged to the expenditures of the Ministry of Environment, Lands and Parks. Had these costs been included, there would have been no net proceeds included for this transaction in the Privatization Benefits Fund.

While the Auditor General questioned the appropriateness of the basis for presenting the financial results of the privatization transactions, he did conclude that, in all material respects, the government accounting for the 46 sales designated by Cabinet complied with the provisions of the Privatization Benefits Fund Act and with the government's stated accounting policies. Our discussions and reviews have found no indications that the policies approved by the Policy Board are not being followed consistently.

- **Proceeds from Gas Division**

During fiscal 1992, the Banking/Cash Management Branch of the Provincial Treasury Board sought to designate certain proceeds from the sale of the Mainland Gas Division of B.C. Hydro as proceeds from a privatization transaction. Approximately $21 million became payable to the Province as a result of the settlement of a deferred payment resulting from the original sale. The deferred payment was to be satisfied by the payment of income taxes to the province and, to the extent not satisfied in that manner, by payment of additional proceeds. The Provincial Treasury has advised that, on advice of counsel, it could not automatically have the funds resulting from the settlement fall within the provisions of the OIC which designated the Mainland Gas disposition as a privatization transaction. Believing that the

settlement payment constituted a "privatization transaction", the Provincial Treasury sought to have the settlement amount to be so designated. Treasury Board staff, however, were not in agreement with the application for designation made by the Provincial Treasury because they viewed the settlement amount as a prepayment of income taxes that would otherwise have been paid to the Consolidated Revenue Fund in any event and had included these payments in the 1991/92 revenue estimates for the General Fund. The Minister of Finance agreed with Treasury Board, thus enabling the amount to become payable to the General Fund.

Had the proceeds from the settlement been payable to the Privatization Benefits Fund rather than the General Fund, the deficit for fiscal 1992 would have been increased by some $21 million.

B. Activities and outputs

1. Major programs

The Fund will continue to receive proceeds from the privatization of road and bridge maintenance contracts, primarily from the lease of equipment to contractors. The amount of proceeds expected over the next three to five years is approximately $4.5 million per year. It may also receive approximately $5.1 million from the sale of the Vancouver Island Gas Operations, provided the transaction is designated as a "privatization transaction". The process to obtain such designation has begun.

WLC Developments Ltd. is expected to generate significant revenues from the disposition of certain Whistler properties (in the range of $60 million to $70 million over the next four to six years). As a wholly owned subsidiary, all its income will be attributable to the Fund.

As outlined above, the Minister of Finance has approved a diversification program for the investments of the Fund monies to encompass venture capital pools and merchant banking pools. The government's investment in the Venture Capital pools will total $20 million, provided matching Venture Capital is provided by the private sector. Its investment in the merchant banking pool will total $10 million. The decision to diversify the investment program to encompass these pools will increase investment risk of the monies allocated to the pools, althought expectations of the Investments Branch of Provincial Treasury are for returns in range of 15% -20% ofater giving effect to possible losses.

2. Expected outputs and benefits

The Fund is not an operating fund and therefore, except for the income earned by it that might be transferred to the General Fund upon the direction of Cabinet by Order-in-Council, its investment returns will not directly benefit the General Fund.

It however, is an integral part of the Consolidated Revenue Fund and its earnings are included in CRF earnings.

C. Implications for government

The Fund was established for the purpose of preserving the capital (revenues) generated by the privatization initiatives and separating it from the ongoing operations of the General Fund. Payments to the Fund from the General Fund are treated as expenditures (revenue reductions) for the purpose of reporting the amount of surplus and/or deficit in the General Fund. Similarly, only income distributed to the General Fund is recognized as revenue by the General Fund.

Were the Fund to be accounted for as part of the General Fund, the reported deficit of government at March 31, 1991 would have been reduced by approximately $500 million, being the equity of the Fund at that date (see Schedule 2). Under the current provisions, it is not possible to account for the Fund assets and/or income as part of the General Fund. However, as recommended in the Accounting Policies issue paper, the government should report on a Consolidated Revenue Fund basis, which would incorporate the activities of the Privatization Benefits Fund.

Appendix B

False Creek Land Sale

A. Background

On May 11, 1988, the province (through BCEC) sold the former Expo lands to Concord Pacific Developments Ltd. (Concord). In return for the land, the province received:

- $50 million cash.
- A non-interest bearing note from Concord ("the Concord note") with the following payment schedule:

$ 10M	May 11, 1995
$ 10M	May 11, 1996
$ 10M	May 11, 1997
$ 10M	May 11, 1998
$ 10M	May 11, 1999
$ 20M	May 11, 2000
$ 40M	May 11, 2001
$ 60M	May 11, 2002
$100M	May 11, 2003

  This series of payments are secured by a promissory note from Concord and an irrevocable letter of credit from the CIBC which expires on June 11, 2003.

- A participating agreement {Public Participation Funding Commitment ("the Commitment")} provides for the province to receive further payments from Concord. The amount of the additional payments are dependent on and are to be calculated with reference to:
  - An index of the changes in Vancouver housing prices from a base established at March 31, 1988.

- The floor space permitted to be developed on the land by the City of Vancouver beyond certain thresholds.

The nominal amount payable under the Commitment will be $10 per square foot for developed floor space (as defined) in excess of 12 million square feet, up to 13.2 million square feet at which time the participation amount will increase to $12.50 per square foot.

These payments are due from Concord on the earlier of:

- Above ground construction on a parcel of land that has exceeded the floor space threshold.

- The closing of the sale of a parcel provided that if the sale takes place before the first rezoning of the separate lot that has exceeded the floor space threshold, then the date of rezoning governs.

This participating agreement is secured for up to $37 million by a letter of credit from the Hong Kong Bank of Canada which expires on January 14, 1993 (the letter is renewed annually).

Discount factors were applied to the Concord note and to the anticipated payments under the Commitment to determine the present value of the expected stream of payments in each case. The present value of these payments, using discount rates in effect on April 11, 1988, was determined to be $145 million; allocated as to $125 million for the cash and the Concord note and $20 million for the Commitment. The full amount (i.e., $145 million) has been recorded as sales revenue. The present value of the Concord note (i.e., $75 million) and the estimated $20 million present value for the Commitment, were recorded as a note receivable and a public participation funding agreement receivable, respectively. As at March 31, 1991 the amortized book value of the note receivable was approximately $100 million. The public participation funding agreement receivable remains at $20 million.

B. Issues

1. Present value of amount receivable under the commitment

The determination of the amount and the timing of the receipt of payments under the Commitment is dependent upon a number of variables including:

- The amount of the developable floor space.

- The timing of the development of or sale of the floor space in excess of the thresholds outlined in the document.

- Residential real estate prices.

On the basis of certain available information, including correspondence from Burns Fry Limited and discussions with the City of Vancouver, as well as information with respect to past increases in Vancouver residential real estate prices, the nominal amounts receivable under the Commitment were estimated to be between $32 million and $150 million. On the basis of discount rates in effect on April 11, 1988, and estimated receipts at the end of 13.5 years and at the end of 18.5 years, present values of the nominal receipts were determined to be in the range of $7 million and $33 million; $20 million was chosen as an appropriate midpoint present value. Independent advice concluded that the $20 million was a reasonable measurement of the amount to be recorded as a receivable from Concord Pacific Developments Ltd.

In a letter dated January 15, 1991, Concord Pacific Developments Ltd. acknowledged to the Ministry of Finance that based on information with respect to changes in Vancouver housing prices and the status of the zoning for the area covered by the Official Development Plan for the Expo lands, their contribution under the Commitment would be approximately $7.4 million. Our review and discussions with the planning department of the City of Vancouver and with Concord indicates that the estimate of liability is in accordance with the provisions of the Agreement and the currently proposed, approved and expected developable area of approximately 12,414,391 square feet. No reference is made with respect to the timing for the payment; however, Concord believes that the liability might become due within a seven to ten year time frame under normal zoning, development and absorption assumptions.

Concord, on the basis of density proposals for the development of two similar properties surrounding the City of Vancouver, believes that it might be possible to increase the proposed developable area by an additional million square feet. However, the required change to the Official Development Plan is highly uncertain at this time.

On the basis of the foregoing information, it is our view that the estimate of the amount receivable under the commitment requires updating on the following basis:

- The excess developable square feet approved under the existing ODP would, if payment were due on December 31, 1990, have resulted in the receipt of $7.4 million.

- The estimated payment date is from seven to ten years; 8.5 years is an appropriate midpoint (9.5 years from December 31, 1990).

- On the basis of house price increases between December 1980 and December 1991, it is reasonable to conclude that the index will reach 1.92 at the time the funds are expected to be received.

- The discount rate of 9.5% (compounded semi-annually), being the Government's current cost of long-term funds, is appropriate.

The value for the receivable at December 31, 1991 calculated under the above updated scenario is approximately $6.5 million.

We recommend the receivable be written-down to $6.5 million; bringing the present value of the receivable into line with the updated estimate of the likely outcome. We further recommend that the amount of the receivable be increased annually by amortizing its recorded value at the annual discount rate of 9.5%.

The additional square feet that might be approved for development should be excluded from the estimate until it is reasonably determined that it will be allowed. If Concord is successful in obtaining approval for the increase in the amount of the developable square feet, it would be appropriate to recognize an increase in the amount of the receivable at that time and to record a gain on the basis of revised estimates.

2. Present value of Concord note

The Concord note contains reference to the discount rates that will apply if the prepayment right is exercised and a formula for calculating the amount of the prepayment. This formula is based on monthly compounding. Annual compounding was used in the calculation of the present value of the note originally. Had monthly compounding been used, the value of the note at its inception would have been $70.74 million rather than the recorded $74.99 million. At March 31, 1991, the amortized book value of the note would have been $95.5 million rather than the $99.9 million that was recorded in the General Fund. At December 31, 1991, the relative amortized book values would have been $103.2 million and $107.6 million, respectively.

The amortized book value of the note should be written-down to more properly reflect the compounding provided for within the note. The written-down value should be amortized at the new discount rate until maturity or prepayment, whatever the case.

3. Disposal process

The government announced the initiation of the process to sell the Expo lands to the private sector in March 1987, at or about the same time as it announced the creation of British Columbia Enterprise Corporation (BCEC) as a result of the merger of B.C. Place Ltd. and B.C. Development Corporation. The legal organization of BCEC did not take place until August 30, 1987 when formal approval was given by Cabinet. BCEC had its own Board of Directors (comprised of senior business leaders and employees of BCEC and included the Minister Responsible), and its own Management Committee. One of the primary mandates of BCEC was to pursue the privatization of its land assets.

The Board of Directors of BCEC, at a meeting held on August 14, 1987, approved certain objectives that were to be achieved in the process to be followed in the disposition of the Expo lands. Its primary objectives were stated as follows:

- To ensure a rapid process leading to an early and successful conclusion.
- To facilitate the privatization of BCEC.
- To limit the uncertainties and residual obligations to BCEC.
- To maximize the total return to BCEC.

The process of identifying potential bidders, contacting them, evaluating the initial bids and subsequent formal proposals and finally, negotiating with the successful candidate was the primary responsibility of the Board which was ultimately responsible to Cabinet which made the final decision. The Board carried out its mandate through several committees which were formed to look after various aspects of the process including:

- The Executive Committee
- The Selection Committee
- The Negotiating Committee

At that time the government announced its decision to sell the Expo lands, it made it clear that the entire site would be sold "en bloc" as opposed to selling the land in its component parcels. Its rationale for wanting to sell the site en bloc was its desire for a single developer to undertake an overall development plan that would ensure compatible uses in various parts of the property. In the Government's view, this would give more flexibility and responsibility to the developer in dealing with City zoning requirements over the whole area. It did not, however, deter individual developers from developing specific parcels of the site once the overall development plan was in place.

The following is a general overview of the process followed:

- World-wide potential participants were identified and contacted through media advertising and/or direct contact. Interested participants were asked to submit written "Expressions of Interest" to participate in the development. A total of 17 written "Expressions of Interest" were received.
- Each of the participants which submitted an "Expression of Interest" was evaluated on the basis of certain specific evaluation criteria established by the BCEC Selection Committee. The evaluation criteria included minimum requirements with respect to:

- financial capability
- track record
- organization
- the effects on privatization of BCEC

► The Board approved a short list of seven candidates, each of which was asked to submit a formal proposal for the development of the Expo lands and the purchase price payable to the government. Only two formal proposals were received. The Concord Pacific Developments Ltd. proposal was judged, on the basis of the pre-established criteria, to be the superior proposal.

Burns Fry Limited, in their letter of March 11, 1988 to the Board of Directors of BCEC, concluded that given the stated objectives of BCEC the process followed was sufficient to solicit offers to purchase the lands from a wide range of parties, domestic and international, that might have interest in such a purchase and the financial capability required to purchase and subsequently develop the lands. It was also their conclusion that given the objectives of the BCEC Board, the Concord Pacific submission was financially superior to that of the other bidder, and it provided more certainty with respect to the receipt of funds.

Our review of the process, while limited in scope, leads us to conclude that, if it was appropriate to sell the land in one block, the process followed was fair to all bidders.

However, having established as an objective that it would limit the residual obligations to BCEC, the arrangements entered into did not meet this objective: those acting on behalf of the Province contracted to assume an open-ended unspecified liability (which could now turn out to cost the Province up to $100 million) by agreeing to undertake site remediation at the Province's cost.

As an observation to this process, and with the benefit of hindsight, there were different options which might have been chosen: with the known uncertainty of cleaning the site, it might have been more prudent to recognize and quantify the risk before selling the property, either in smaller lots or in one large lot.

Appendix C

Mainland Gas Division (B.C. Hydro) Sale, 1988

A. Introduction

The purpose of this report is to provide a brief summary of the sale process which led to the transfer of Mainland Gas, a division of B.C. Hydro, to Inland Natural Gas Co. Ltd. This was one of the property transfers under the government privatization process in 1988.

It is important to note that the process for the Mainland Gas Privatization was determined by the Provincial Government through its Privatization Advisory Committee (B.C. Hydro). B.C. Hydro's Board and management did not control the initial identification of what was to be privatized nor the sale process. Operating under a directive from government instructing the Board of B.C. Hydro to sell the Gas Division, B.C. Hydro's management assisted the Privatization Advisory Committee in the sale process.

Our comments are based on information obtained through interviews of individuals who were directly involved in the sale process and a review of selected documents which were made available to us. In light of the fact that this process took place over three years ago and that our review did not include verification of the details provided, the information outlined in this report, while substantially correct, may not fully correspond to the exact events as they occurred.

B. The presentation of the assets for sale

The decision to offer selected units of B.C. Hydro for the sale to the private sector was made by the government of B.C. following a report by a consulting firm on this subject. Four divisions of B.C. Hydro were identified for privatization sale; among them, Mainland Gas. This identification work took place in 1987.

In early 1988 the government formed a "Privatization Advisory CommitteeB.C. Hydro" (PAC) under the chairmanship of Mr. Dale Parker. The committee's responsibilities were to define and spearhead the process to identify interested parties and present Cabinet with a short list of bidders for the purchase of the four B.C. Hydro units—Mainland Gas, Victoria Gas, the Rail Division and Research and Development.

PAC was composed of more than twenty individuals with very reputable credentials identified specifically for their skills and knowledge. Their background varied from the private sector to government ministries and B.C. Hydro management. Some of the key individuals involved are listed in Schedule A to this Appendix.

Four sub-committees reporting to the PAC were formed, each specifically focused on one of the four B.C. Hydro divisions targeted for sale.

The first task was to advertise the existence of this opportunity in order to identify potential interested parties in the business community, not only within B.C. but also in the broader economic setting of North America and other industrialized countries.

This objective was achieved by issuing an information document called "A business opportunity" which was distributed widely and made available to all interested parties. In addition, advertising in local and national newspapers was carried out and a large number of consulting and brokerage houses were visited to introduce this sale opportunity, including specific trips to Toronto and New York.

C. Screening bids

More extensive information ("An information memorandum") was provided to prospective purchasers to allow them to make preliminary bids. These bids were analyzed with the intent of creating a short list of serious bidders who would be permitted to gain more detailed information before submitting a final bid. At this stage, the prospective purchasers' credentials and preliminary proposals were assessed against the sale criteria defined in the information memorandum. These were:

- price
- ownership structure
- privatization objectives:
    - economic development
    - job protection
    - employee ownership
    - cost effective service
    - operational safety
    - management expertise
    - financial strength

Emphasis was placed on the financial strength of the bidders to limit the number of interested purchasers to the ones who appeared to have financial ability to carry out a large acquisition.

During all phases of this process, and particularly while assessing the prospective preliminary bids, sub-committees were formed to draw on the specific expertise of the members of PAC to ensure that an effective and objective analysis of the bids was conducted.

We are advised that a summary report of the nine preliminary bids for Mainland Gas was presented to Cabinet. This report, while presenting all preliminary bids, recommended five bids be included in the final short list. The short list of bidders was then announced. Schedule B lists the nine preliminary and the final five bidders.

One of the five bidders withdrew voluntarily prior to the submission of the final bids. The remaining four short listed bidders were then given access to more detailed information and allowed a private two day question and answer session with members of PAC and B.C. Hydro. A written transcript of each question and answer was provided to every bidder. Based on this information, final bids were then submitted to PAC.

A detailed analysis of the final bids for Mainland Gas was carried out using the same criteria followed at the preliminary phase. This evaluation also included discounting the purchase price to a present value for any deferred payments.

We understand that a summary report was presented to B.C. Hydro's board of directors for comment and then to Cabinet. At this stage, no recommendation was put forward to Cabinet. Based on PAC's report to Cabinet, Inland Natural Gas Co. Ltd. was selected by Cabinet as the preferred bidder. Prior to announcing this selection, the other four bidders and the media were given summary information of each of the bids on a no name basis.

D. The final negotiations

Final negotiations were carried out at this stage with the preferred bidder. The structure of the transaction was defined and all relevant agreements drafted and finalized. This final phase took place over approximately two months, with closing to take effect on September 30, 1988.

The net assets of Mainland Gas were transferred to a separate numbered corporation, under the beneficial ownership of the Province of B.C. (later named B.C. Gas), whose shares were subsequently sold to Inland Natural Gas. Proceeds on the sale were $786 million including $44 million of deferred proceeds against which provincial income taxes otherwise payable would be applied. Details on the nature of the proceeds and their distribution and allocation are outlined in Schedule C.

As part of the overall agreement, B.C. Hydro and Inland Natural Gas also negotiated a number of service agreements including administration and billing services and research and development services. Fee schedules were agreed upon to define the appropriate payment terms for the services provided.

In addition, B.C. Hydro represented to Inland Natural Gas that it had no knowledge of hazardous substances or waste which, by virtue of the sale, would become the responsibility of Inland Natural Gas. B.C. Hydro agreed to share in the clean up costs of such polluting substances or waste, should any be found subsequent to the date of the sale, on a 50/50 basis with the exception of PCB's whose removal costs would be fully borne by B.C. Hydro.

E. Summary observations

PAC's mandate was not to select the ultimate buyer, but to provide a means to identify qualified prospective purchasers, to analyze and assess bids received against stated criteria and objectives and to offer Cabinet the tools to make the most informed decision possible.

Throughout this sale process, PAC appeared to maintain a direct focus on public openness. The Advisory Committee conveyed its findings and analysis to B.C. Hydro's board of directors for comment and to Cabinet for a decision. It appears process followed by the Advisory Committee met the criteria established at the outset with respect to the Mainland Gas sale.We have not conducted a detailed review or valuation and therefore are unable to be specific about the price obtained on the sale. Additional study would be required to determine whether the price was reasonable.

Key Members of the Privatization Advisory Committee (B.C. Hydro)

Schedule A

William A. Bakk	Partner, Touche Ross
Larry Blain	Vice President & Director, Manager Corporate & Government Finance Department, Pemberton Securities Inc.
Michael Costello	Assistant Deputy Minister of Provincial Treasury, Ministry of Finance
David Craig	Assistant Controller, B.C. Hydro
J. Bruce Hodge	Vice President Corporate Finance, Pemberton Securities Inc.
Doug R. Johnson	Partner, Owen Bird
Dave Laundy	Vice President & General Manager, Comcore Public Affairs
Ed R. MacGregor	Assistant Deputy Minister, Ministry of Energy, Mines & Petroleum Resources
Brian Neal	Ministry of the Attorney General
Dale G. Parker	Committee Chairman and President & C.E.O., B.C. Bancorp
R.S. Plecas	Deputy Minister, Ministry of Energy, Mines & Petroleum Resources
John Sheehan	Vice-President, Finance, B.C. Hydro

Privatization Advisory Committee (B.C. Hydro)
List of Bidders for Mainland Gas Division

Schedule B

Company Name	Preliminary list	Short list
B.C. Energy Inc.	x	x
B.C. Gas Group	x	
Inland Natural Gas Co. Ltd.	x	x
Inter-City Gas Corp.	x	x
Pacific Rim Gas Inc.	x	x (1)
Pan Pacific Utilities Corp.	x	x
Peoples Natural Gas Co Ltd.	x	
Southwest Gas Corp.	x	
Synex International Inc.	x	

(1) withdrew prior to final bid

Privatization Advisory Committee (B.C. Hydro)
Mainland Gas Division
Sale Proceeds Allocation

Schedule C

	(in millions)	Comments
Gross sale proceeds	$ 786	
Less: deferred tax proceeds	44	Settled in 1991
	$ 742	
Composed of:		
Debt vendor financing, repayable over five years in equal yearly instalments, bearing interest semi-annually at the Province of B.C. borrowing rate plus .25% per annum, secured by a first fixed charge over the assets sold.	$ 300	1992 and 1993 instalments of $120 million remain payable
Exchangeable redeemable debenture, redeemable over two years starting twelve months after the closing, exchangeable for common shares of the purchaser at the option of the Province.	150	Refinanced by issuance of exchangeable bonds
Cash on closing	292	
	$ 742	
Allocated as follows:		
Retained by B.C. Hydro:		
Net book value of assets sold	$ 434	
Financing costs		
Operating loss to date of closing	12	
Additional assets	8	
Sales taxes	5	
Privatization, pension and financing costs	33	
	492	
Paid to government	250 *	
	$742	

*An additional $11 million was paid to government as a result of the privatization of the Rail Division. To March 31, 1991, approximately $238 million of the $261 million has been paid to the Privatization Benefits Fund (see separate report). The balance was used to pay for costs incurred by government in the financing of the privatization and to fund obligations (primarily pension costs) assumed by government as a result of this privatization.

Appendix D

W.L.C. Developments Ltd.

A. History and mandate

W.L.C. Developments Ltd. ("WLC" or "the Company") is a company established under the Company Act of British Columbia in January 1983 by the Province of British Columbia. The sole shareholder is the Minister of Finance and Corporate Relations. The Ministry of Environment, Lands and Parks has management responsibility for WLC and two of its senior personnel are Directors. Mr. James Switzer, the third Director, also acts as President. WLC's staff consists of the President and a part-time project manager, accountant and secretary, all of whom are under contract. This equates to about 2.8 FTEs.

WLC was created when the Resort Municipality of Whistler (the "Municipality") required financial assistance in developing the Whistler Conference Centre and Golf Course. WLC was created by the Province to assist in the development of Whistler as a world class destination resort by completion of the Whistler Conference Centre and Golf Course and other infrastructure and by sale of the remaining development sites in the Whistler Town Centre. Under the "Business Proposal Agreement" of 1988, the groundwork was laid for WLC to obtain development rights both for its 33 acres of Whistler Village North and for the adjacent 25 acre parcel which was occupied by the Myrtle Philip School. Under the "School Relocation Agreement" of 1989, WLC committed to fund the cost to relocate the existing school facilities in return for acquiring title to the 25 acre parcel occupied by the School. The 25 and 33 acre parcels together make a 58 acre area that is now known as Whistler Village North.

WCL also holds title to approximately 100 acres of land known as the Blackcomb Benchlands, which are under option to purchase in favour of Blackcomb Skiing Enterprises Ltd. until 2004. This option is held by Blackcomb as an adjunct to its ski area development agreement with the Province.

B. Current financial situation

At October 31, 1991, the main asset on WLC's balance sheet was property held for sale of $22.9 million. This amount consists principally of the cost of acquiring and developing the 58 acre Whistler Village North site. The amount includes the estimated

$5.3 million funding required to move the School (in essence, the cost of acquiring the 25 acre parcel). Of the $5.3 million, $3.9 million has been expended and $1.4 million has been accrued as a liability.

In June 1990, an independent appraisal of the Whistler Village North site estimated the market value at $22 million. In 1990, no site servicing had been completed. This appraisal assumed that WLC would pay for the School relocation and that the lands would be sold unserviced and unsubdivided. In 1990, a decision was made to subdivide and service the lands and to sell serviced parcels. At October 1991, about half of the site servicing had been completed. It is WLC's intention to install roads and all off-site services and then market zoned lots for a variety of uses. The Company's internal projections suggest that Village North will produce gross revenues of $60 to $70 million over a four to six year period. If expected prices are achieved on all the remaining lots in Whistler Village North, it is reasonably assured that proceeds will exceed development and acquisition costs.

WLC has arranged with the Province for up to $7 million of short term borrowings by the issue of commercial paper. At October 31, 1991, $6 million of short term debt had been incurred. The $1.4 million accrual for school relocation costs and the short term debt are WLC's main liabilities on its financial statements. It has a shareholders' equity position of $16.9 million.

C. Marketing

In July 1991, the marketing of Whistler Village North was launched with a major international advertising campaign. This effort, together with previous marketing, has resulted in a registration list of about 700 interested parties. When each lot is brought forward for sale, national and local advertising is performed and a mailing is sent to the registrants. WLC does not publish an asking price but does establish an estimate of value by means of independent appraisal to assist in evaluating offers.

Currently, WLC has completed the sale of Lots 28 and 29 (both zoned residential), and has publicly invited submissions of offers to purchase Lots 11 to 16 for a mixed shopping centre and residential development. A great deal of interest has been expressed in this site.

D. Accounting treatment of the WLC entity

At March 31, 1991 WLC's property held for sale had a cost of $18.0 million. A reconciliation of the PBF's asset accounts at March 31, 1991 performed by staff in the Provincial Treasury office show that the assets of WLC are reflected in the PBF financial statements at a market value of $23.8 million. This market value appears reasonable based on the current market for the lots as discussed in the previous sections.

The province's interest in WLC is recorded in the Consolidated Revenue Fund financial statements at no value and in the Summary Financial Statements at its modified equity value of $17 million.

Appendix E

Duke Point Development Ltd.

A. Description

1. Mandate

Duke Point Development Limited (Duke Point) is a company established under the Companies Act in 1978 by the British Columbia Development Corporation (BCDC) to undertake the development and marketing of a major industrial park on 350 acres of waterfront land in Nanaimo. The development is located on a spit of land to the east of the Nanaimo River estuary, just north of a Hooker Chemical plant and MacMillan Bloedel's Harmac pulp mill. Approximately $35 million was expended to acquire the land, grade the site, fill in tidal flats and create a deep sea port. Duke Point was envisaged to be the site of two major pulp mills, other forestry related industrial plants and a deep sea port.

2. Size of organization

Duke Point has no employees and no FTEs. Staff of the Vancouver Island Region office of the Ministry of Environment, Lands and Parks operate Duke Point. A Regional Director is in charge of operations.

3. Legal basis

Duke Point was incorporated under the Companies Act in 1978. All its shares were owned by BCDC. In the late 1980's BCDC assets, including Duke Point, were transferred to the British Columbia Enterprise Corporation (BCEC). In 1989 BCEC was dissolved and Duke Point was transferred to the Province. The Minister of Finance and Corporate Relations is the sole shareholder of Duke Point; he holds the shares for the benefit of the Privatization Benefits Fund. Senior staff of the Ministry of Environment, Lands and Parks have been appointed as Directors to operate Duke Point.

4. Recent history

The development of the site was completed in the early 1980s and 25 serviced lots ranging in size from 5 to 60 acres were brought onto the market under less favourable economic and political conditions than existed at the time of the project's

conception in 1978. As a result little development has occurred beyond the initial phase of the Nanaimo Harbour Commission's deep sea port facilities (one shipping berth and one barge ramp) and Doman Industries' (Doman) two sawmills. Doman purchased one lot and currently leases a second and a portion of a third lot on which the sawmills are located.

Two pulp mills were intended to be the anchor tenants of the industrial park which would in turn attract more industry. Plans for the pulp mills were scrapped in the early 1980s for a host of reasons beyond the scope of this study. This was the initial factor that adversely affected the marketability and value of the development. Through the 1980s Duke Point's marketing policies priced the lots at cost (in aggregate $35 million) which left the prices substantially above market values. This policy was motivated by the government's desire to recover the cost of development and maintain the image of a successful development. This impeded sales of the lots and the industrial park remained largely undeveloped.

5. Reporting and accountability

The Ministry of Environment, Land and Parks has management responsibility for Duke Point and two of its senior personnel are Directors.

Duke Point is accounted for as part of the Privatization Benefits Fund.

6. Management Issues

Interest of B.C. Ferry Corporation

At present Lots #20, 24 and 27 are not being marketed as the British Columbia Ferry Corporation (BC Ferries) has expressed an interest in relocating its Mid-island ferry terminal from Departure Bay in downtown Nanaimo to Duke Point. Such a project would involve the construction of a highway connector to the Island Highway. Management of Duke Point does not know if such a plan would increase the desirability of Duke Point lots. However, neither B.C. Ferries nor Duke Point has studied the relocation plan in any depth and its potential impact on the Duke Point industrial park cannot be quantified. The management issue is the apparent lack of co-ordination between Duke Point, B.C. Ferries and the Ministry of Transportation and Highways; although it is not clear how this has arisen.

B. Activities and outputs

Duke Point's main activity is to market for sale the remaining 21 lots. Until all lots have been sold the administration of the industrial park, including lots under lease, is a second purpose.

The Board of Directors has adopted all Crown Lands policies in dealing with Duke Point. The resultant lot pricing policy requires that they be sold subject to independent appraisal. Management has established asking prices that are in excess of the appraised values. Management of Duke Point can accept any offer that comes within 15% of the appraised prices. This pricing policy gives management of Duke Point a fair degree of room to negotiate lot sales. During the Summer of 1991, one lot was sold for $230,000 which was $24,000 below its appraised (and carrying) value. Two lots are currently under option until May 1992 and are carried on the books at their option prices.

The eventual success of the project now rests on demand for heavy industrial and industrial zoned lots in the mid-island area, an external factor over which the provincial government has little control. Accordingly, the eventual sale of all the lots in the industrial park could take a very long time to achieve. The benefit of this project is meant to be increased economic activity in the mid-island area and the resultant positive effect on employment and tax base.

C. Resource base

Duke Point has a Balance Sheet with $13.5 million of assets. Forecasted expenditures are under $500,000 per year for the foreseeable future. Future revenues are substantially dependent on lot sales, which are not easily forecast. Lease revenue, in the range of $600,000 per year, is provided by the two leases with Doman which run ten years (including renewal options) from June 15, 1988.

Five Year Picture ($000)

	Actual		Forecast		
	1989/90	1990/91	1991/92	1992/93	1993/94
Budgeted Expenditures	$535	$391	$400	$400	$400
Statutory Expenditures	-	-	-	-	-
Special Accounts and Funds	-	-	-	-	-
Subtotal	535	391	400	400	400
Financing Transactions/Loans, etc.	-	-	-	-	-
Revenue	786	615	600	600	600
Proceeds from lot sales	-	-	230	?	?
Net Cost/Contribution	251	394	430	200	200
Write-down of property held for sale	2,617	-	459	?	?

D. Issues

1. Valuation of assets

In general, the lands held by Duke Point are valued at the lower of cost or net realizable value. Between 1984 and March 31, 1990, a total of $14.25 million in provision for write-down of the carrying value of the property has occurred. No write-down occurred in fiscal 90/91.

The item described as "property held for sale" consists of all lots except those leased to Doman. Net realizable value of property held for sale at March 31, 1991 of $8.82 million has been based on independent appraisals dated October 26, 1989 and February 15, 1990. As at August 1, 1991 all of the lots except Lot #24 (which is one of the lots B.C. Ferries is interested in) were reappraised by independent appraisal at a market value $459,000 below their previous appraisals. **This suggests that a further write-down on these lots in the fiscal 91/92 year is likely appropriate.** Lot #24 which made up $1.665 million of the March 31, 1991 carrying value has not yet been reappraised.

In the financial statements the item described as "net investment in sales-type leases" is in fact the lots leased to Doman. These properties are carried on the balance sheet at the option price at which Doman may acquire the properties. Since Doman has built plants on these lands and since Doman exercised such an option on a third property in June, 1989 management of Duke Point believes it is likely that Doman will exercise these purchase options before the end of the leases, being June 1998.

A further concern of the valuation of "property held for sale" is the method of determining market value. The appraisal reports properly base the market values on comparable sales of industrial properties in B.C. However, since the absorption rate of industrial lots in the Nanaimo area could be very slow, recognition of the time value of money could be taken into account, which could cause the net present value (NPV) to be substantially lower. A "Report to Shareholder" prepared by management of Duke Point calculated an NPV of $7.9 million based on a set of hypothetical assumptions. A set of more pessimistic assumptions (essentially more protracted lot sales) produced an NPV of $5.5 million. This produces a range of NPV's of $5.5 million to $7.9 million, which is below the carrying value of $8.82 million, suggesting the economic value of the lots does not currently exceed their carrying value. Historical cost accounting does not contemplate write-downs based on net present value calculations but on net recoverable amounts. Accordingly no further write-down is recommended as the current write-down policy meets generally accepted accounting principles.

2. Future site servicing costs

The entire site, with the exception of 24 acre Lot #20, has been serviced with paved access roads, power, water and sewer. The present sewer system is a package

treatment plant with limited capacity. If companies requiring considerable sewage capacity locate in the park or as the park approaches full occupancy greater sewage treatment capacity may be required. Adding capacity would involve constructing a major sewage disposal line to the City of Nanaimo or Regional District's system. This cost was estimated in 1990 at $4.0 million. It is not certain that this hook-up will be required. Ultimately, this will become known when the industrial park approaches full occupancy. It is not clear who would bear this cost: Duke Point, the lot owners or the City of Nanaimo. Management of Duke Point have taken the position that companies necessitating the construction of the hook-up because of their large sewage capacity requirements should bear the cost of the line. If either Duke Point or the lot owners must bear this cost then value of the project may be negatively impacted either by direct cost to Duke Point or decreased lot prices that purchasers will be willing to pay.

E. Accounting treatment of the Duke Point Entity

Duke Point is an asset of the Privatization Benefits Fund (PBF). Assets of the PBF are treated as a portfolio of investments and are accordingly accounted for on a market value basis. A reconciliation of the PBF's asset accounts at March 31, 1991 performed by staff in the Provincial Treasury office show that the assets of Duke Point are reflected in the PBF financial statements at market value, being the carrying value of the assets.

The Province's Summary Financial Statements (SFS) combine the General Fund, the PBF and the Budget Stabilization Fund with those of other Government organizations and enterprises. Note 6 to the SFS shows Duke Point carried at $4 million. This amount is the $3.665 million item on the Duke Point financial statements described as "Due to Province of British of British Columbia." The province has effectively written off its 50% portion of the $13 million IDSA Loan. Therefore the carrying cost of Duke Point of $3.665 million is reasonable as the market value of the Duke Point entity is almost certainly in excess of this amount once the IDSA Loan has been written off.

We recommend a write-down of $459,000 for decline in market value of property held for sale. See section "Valuation of Assets" for discussion.

F. Potential future impacts

1. Cost drivers

The most significant ongoing cost is property taxes which currently are in the range of $200,000 to $250,000. This was reduced from $393,000 in fiscal 1989/90 because of the decline in assessed value of the properties.

Duke Point currently pays a "grant in lieu of taxes" to the City of Nanaimo which is considerably less than that which would be paid by a land holder in the private

sector. However, the risk of Duke Point being forced to pay "regular" property taxes is low given the ongoing difficulties facing the industrial park.

2. Impact on forecasts

Lot sales, which are unpredictable, impact forecasts.

3. Lurking expenditures

See section "Future Site Servicing Costs".

G. Implications for government

1. Revenue maximization strategies

Marketing plans for 1992 include national and international advertising and the listing of lots with real estate agents. The lots have not been marketed with any vigor since 1988. A more concerted marketing effort may increase the rate of lot sales.

2. Expenditure reduction strategies

None to suggest, as Duke Point is already operated in a lean fashion.

3. Program redesign options

The government should perform an analysis of the cost of continuing to hold, manage and operate the industrial park compared to potential future revenues from lot sales. If the long-term outlook does not look bright, the government should reevaluate its lot pricing policy. The benefit to government of lowering pricing to promote current lot sales and thereby reduce ongoing program costs is an analysis that should be performed.